# 2005

# ANNUAL REPORT

Beaumont Select
CORPORATIONS

BEAUMONT SELECT CORPORATIONS INC.

## NOTICE OF ANNUAL MEETING

Beaumont's Annual Meeting of holders of common shares will be held in the Borden Ladner Gervais LLP board room at 1000, 400 Third Avenue S.W. at Calgary, Alberta at 11:00 a.m., Calgary time on Tuesday, December 20, 2005.

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# Corporate Directory

### DIRECTORS

Winston Ho Fatt
Andrew Hyslop
Peter Kreutzer
Bruce Dorset

### TRANSFER AGENT

Computershare Trust
Company of Canada
Calgary, Alberta

### LEGAL COUNSEL

Borden Ladner Gervais LLP
Calgary, Alberta

### HEAD OFFICE

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### OFFICERS

Winston Ho Fatt
*Chairman of the Board, and*
*Chief Executive Officer*

Bruce Dorset
*Vice Chairman of the Board*

Andrew Hyslop
*Corporate Secretary*

### AUDITORS

Meyers Norris Penny LLP
Calgary, Alberta

### BANKERS

National Bank of Canada
Calgary, Alberta

### STOCK EXCHANGE LISTING

TSX Venture Exchange
Calgary, Alberta

### STOCK SYMBOL

BMN.A

# Corporate Profile

Beaumont Select Corporations Inc. is a management and investment corporation, which has investments in the food processing and real estate industries as well as in a portfolio of marketable securities. Beaumont charges fees and interest on its investments to its subsidiary companies.

### Food Processing Division

The Food Processing Division concentrates on providing high quality private label and branded products of a specialty nature in the frozen food and bakery products sectors. These products are distributed to food wholesalers and retailers in North America including most major retail chains. The Frozen Food Unit is the largest processor of perogies and the largest private label processor of panzarottis in Canada, on a poundage basis. The Bakery Unit has fine product lines including high quality undecorated slab cakes, icings, Christmas cakes, Nanaimo bars, layered cakes, Swiss and jelly rolls, cake and yeast doughnut products, berry cups, crumbs and croutons, mini muffins, handcrafted cookies and sandwiches. Approximately 10% of the sales are made in the U.S.A. The production facilities are all located in Western Canada.

### Investment Division

In an effort to diversify and ultimately enhance the Corporation's sources of income and financial returns, a few years ago the Corporation established a portfolio of marketable securities overseen by the Company's investment division. The investment division operates within investment guidelines established by the Board of Directors of the Corporation and reports to the investment committee of the Board. By June 30, 2005, the Corporation's equity in the portfolio had grown to approximately $11.9 million. In addition to benefiting from the returns obtained in the Corporation's own portfolio, the Corporation also benefits from the investment activities of Somerset Properties Ltd. in which the Corporation has a 40% interest.

### Real Estate Division

The Real Estate Division owns three industrial buildings, one in Winnipeg and the other two in Calgary, with a total area of approximately 110,000 square feet. These buildings are leased to and used by the Food Processing Division. The Corporation also is involved in real estate through its 40% interest in Somerset which latter company owns 91 acres of investment land close to high end residential developments in Calgary. Somerset also owns 52% of Talisman Homes Ltd., a private home building company, giving the Corporation an indirect 20.8% interest in Talisman.

The Real Estate division also looks for developed and undeveloped real estate acquisition opportunities that can assist in the improvement, diversification and enhancement of the Corporation's financial returns.

## CORPORATE GOAL

The corporate goal of Beaumont Select Corporations Inc. is to increase operating income, net income and EBITDA by at least 5% on an annualized basis over a 6-year period and to enhance long-term shareholder value. While Beaumont has historically sought to achieve a higher recurring increase in operating income, reductions in growth potential in the food area over the last two years and anticipated for the next year or two has required a tempering of this objective.

The chart below shows the progress we have made over the past six years.

**FINANCIAL HIGHLIGHTS** (in thousands of dollars except share and per share information)

| | **2005** | 2004 | 2003 | 2002 | 2001 | 2000 |
|---|---|---|---|---|---|---|
| Net Sales | **$ 39,741** | $ 37,575 | $ 36,311 | $ 36,602 | $ 35,026 | $ 32,127 |
| Operating Income | **293** | 385 | 1,525 | 1,109 | 1,411 | 1,456 |
| Net Income | **3,314** | 1,783 | 98 | 83 | 652 | 417 |
| Net Income per share – basic | **0.19** | 0.10 | – | – | 0.04 | 0.02 |
| Funds from operations | **2,133** | 2,343 | 3,199 | 2,232 | 3,150 | 3,072 |
| Funds from operations per share – basic | **0.12** | 0.13 | 0.18 | 0.12 | 0.17 | 0.16 |
| EBITDA before one-time expenses[1] | **7,228** | 5,003[2] | 4,251[2] | 3,727 | 4,100 | 3,108 |
| EBITDA per share – basic | **0.41** | 0.28 | 0.24 | 0.21 | 0.22 | 0.16 |
| Total Assets | **52,109** | 36,614 | 29,142 | 29,679 | 28,116 | 25,196 |
| Total long-term financial liabilities | **10,373** | 9,776 | 9,236 | 8,757 | 8,050 | 8,250 |
| Shareholders' Equity | **14,748** | 11,746 | 10,763 | 10,921 | 11,086 | 10,100 |
| Cash dividends declared per share | – | 0.028 | – | – | – | – |
| Shares outstanding, end of period | **17,449,897** | 17,669,973 | 17,866,473 | 18,139,473 | 18,523,973 | 19,344,473 |

Note 1: EBITDA is earnings before interest, taxes, depreciation, amortization and special one-time expenses.
Note 2: Investment write-offs of approximately $92,000 and $705,000 have been excluded from the EBIDTA in 2004 and 2003 respectively.

# Report to Shareholders

The fiscal year ended June 30, 2005 produced the strongest financial returns for the Corporation in its history measured in terms of sales, net income and EBITDA. These strong results occurred in the face of a challenging product sales market, an appreciating Canadian dollar and strongly rising materials and energy costs.

The strong returns were lead by the Investment Division which included $3.1 million of realized gains and distribution income after margin loan interest (excluding any contribution from Somerset Properties). The Corporation's Food Division achieved a material increase in sales and continued good cash flow for the Corporation though funds flow from operations was materially lower than prior years, especially as a percentage of sales.

The Corporation's own business activities were further enhanced with the material contribution to net income and EBITDA from its investment in Somerset Properties, which accounted for 20% and 9% of Beaumont's net income and EBITDA respectively.

## FINANCIAL HIGHLIGHTS

The Corporation's financial results for the year and the three months ended June 30, 2005 compared to the same period last year included the following:

- Annual sales increased 6% to $39.7 million due to a 9% increase in Bakery Unit Sales partly offset by a 2% decrease in Frozen Food Unit sales. Fourth quarter sales increased $1.4 million or 20% to $8.6 million in the traditionally slow fourth quarter.
- Annual cost of sales increased to $35.5 million due to higher input costs as well as higher sales. Operating margin declined by $0.4 million to $2.8 million or 7% of sales compared to 8.5% for the prior fiscal year. Fourth quarter operating margin increased $0.15 million to $0.6 million or 7.1% of sales compared to 6.3% for the same quarter last year.
- Operating income for the year decreased by $0.1 million to $0.3 million though the operating loss for the recently completed fourth quarter alone was smaller than for the fourth quarter of last year. These fiscal year results occurred despite a reduction of $0.4 million in operating expenses from termination of a royalty payable to a third party.
- Investment portfolio generated a 62% return for the year on opening equity including both distribution income and realized capital gains due mainly to the strength of the Corporation's energy sector investments. Investment income and realized gains increased by $1.4 million to $3.1 million after interest on margin loans compared to $1.7 million in the prior fiscal year.
- Income for the year from Beaumont's 40% interest in Somerset Properties increased to $0.65 million principally from the latter's investment income compared to $0.15 million in the prior fiscal year.
- EBITDA for the fiscal year increased 47% to $7.2 million ($0.41 per basic share) from $4.9 million ($0.28 per basic share). EBITDA for the fourth quarter increased 13% or $0.1 million to $1.0 million ($0.06 per share).
- Annual tax expense increased 142% to $0.7 million, $0.3 million (43%) of which is expected to be current taxes
- Net income for the year increased by $1.5 million or 86% to $3.3 million ($0.19 per share) compared to $1.8 million ($0.10 per share) for the prior fiscal year. Net income for the fourth quarter decreased by $0.2 million to a nominal loss of $0.01 million.
- The book value of the Corporation's portfolio grew $15.0 million to $25.4 million (or 146% since June 30, 2004) and the corresponding margin loans increased $11.5 million to $18.0 million (or 177% since June 30, 2004).
- The Corporation secured two new loan facilities in the third quarter for an aggregate of $1.9 million to refinance prior equipment purchases and for investment in the marketable securities portfolio. The total long term debt at June 30, 2005 increased $0.6 million or 6% to $10.4 million compared to $9.8 million at June 30, 2004, however the current portion of long term debt was reduced by $0.2 million or 16% compared to June 30, 2004.
- Accounts receivable declined by $0.5 million or 14% due to improved collections and bank indebtedness was also reduced by $0.3 million or 10%. Overall, the Corporation's working capital ratio remained unchanged from June 30, 2004 at 1.29 times.
- Shareholders' equity at June 30, 2005 increased 26% to $14.7 million.

## 2005 FINANCIAL HIGHLIGHTS (in thousands of dollars except share and per share information)

| | Three Months Ended | | Year Ended | |
|---|---|---|---|---|
| | 30-June-05 | 30-June-04 | 30-June-05 | 30-June-04 |
| Net sales | $8,576 | $7,178 | $ 39,741 | $ 37,575 |
| Operating Income | (292) | (403) | 293 | 401 |
| Net Income | (12) | 200 | 3,314 | 1,784 |
| Net Income per share – basic | (0.00) | 0.01 | 0.19 | 0.10 |
| Net Income per share – diluted | (0.00) | 0.01 | 0.19 | 0.10 |
| Funds from operations | 331 | 127 | 2,133 | 2,343 |
| Funds from operations per share – basic | 0.02 | 0.01 | 0.12 | 0.13 |
| Funds from oeprations per share – diluted | 0.02 | 0.01 | 0.12 | 0.13 |
| EBITDA | 973 | 836 | 7,228 | 4,912 |
| EBITDA per share – basic | 0.06 | 0.05 | 0.41 | 0.28 |
| EBITDA per share – diluted | 0.05 | 0.05 | 0.40 | 0.27 |
| Total Assets | | | 52,109 | 36,614 |
| Total long-term financial liabilities | | | 10,373 | 9,776 |
| Shareholders' Equity | | | 14,748 | 11,746 |
| Cash dividends declared per share | | | – | 0.028 |
| Shares outstanding, end of period | | | 17,449,897 | 17,669,973 |

## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following Management's discussion and analysis (MD&A) of the results for the year ended June 30, 2005 (referred to as 2004-5) and for the three months ended June 30, 2005 (referred to as the fourth quarter) should be read in conjunction with the Corporation's audited consolidated financial statements for the year ended June 30, 2005 and the accompanying notes. All financial information is reported in accordance with Canadian generally accepted accounting principles (GAAP) unless noted otherwise. The financial measure of earnings before interest, taxes, depreciation and amortization (EBITDA) or funds from operations referred in this MD&A do not have a standardized definition prescribed by GAAP and are therefore not readily comparable to similar measures presented by other corporations even in the same industry. The Corporation's method of calculating EBITDA and funds from operations may not be comparable to similarly titled amounts reported by other issuers. We believe these earnings measures are useful supplemental measures of performance, as they provide investors with an indication of the amount of cash available for reinvestment or distribution to shareholders. Investors should be cautioned, however, that EBITDA and funds from operations should not be construed as alternatives to using net income as a measure of profitability or the statement of cash flows as a measure of liquidity and cash flows.

## CONSOLIDATED FINANCIAL ANALYSIS

### Revenues

Overall revenues increased 7.1% to $39.7 million in the 2004-5 fiscal year from $37.6 million for the same period in 2003-4. The increase resulted primarily from a 9% increase in sales in the Bakery Unit from First City Gourmet Foods (acquired in early August), improved sales from its specialty foods producer Olympia Mills and new product lines. The Frozen Food Unit sales were essentially flat with a 2% increase in sales during 2004-5 compared to the same period last fiscal year. Positive factors for the Frozen Food Unit such as increasing sales from certain new product lines, some price increases and special promotions by certain customers were offset by reduced sales of historically strong products, loss of three US accounts and reduced US sales due to a stronger Canadian dollar versus the US dollar. The stronger Canadian dollar also impacted the Bakery Unit sales for the First City Gourmet products which have not been as robust as initially anticipated. Sales of the historic Bakery Units products continue to face pressure from the desire of customers to reduce carbohydrate consumption.

During the three months ended June 30, 2005, revenues increased 19.5% to $8.6 million compared to $7.2 million for the same period last fiscal year. The increase was derived from a 34% increase in sales in the Frozen Food Unit in what is usually a slow quarter combined with a 9% increase in sales from the Bakery Unit due to the addition of First City Gourmet sales. The increased Frozen Food Unit sales were attributable to special promotions during the quarter by certain customers combined with some increases in sales in certain new product lines introduced late 2003-4.

### Operating margin

The operating margin in 2004-5 of $2.8 million or 7.1% of sales was lower than the $3.2 million or 8.5% of sales achieved in 2003-4 despite the strong increase in sales in 2004-5. The operating margin for the three months ended June 30, 2005 was $0.6 million or 7.1% of sales compared to $0.5 million or 6.3% of sales for the same period last fiscal year. For the 2004-5 year and for the last quarter of that year the decline in operating margin was mostly attributable to the Frozen Food Unit whose historically stronger margins compared to the Bakery Unit were materially affected by the appreciating Canadian dollar relative to the US dollar combined with increased input ingredient, energy and transportation costs. The Bakery Unit was better able to control packaging and material cost but its operating margin also declined during the year due to increased labour costs and certain inventory charges.

### Financing expenses

Interest on long-term debt during 2004-5 was essentially unchanged with the 6% increase in principal amount outstanding offset by slight decreases in rates during the period compared to those in 2003-4. Short term interest and bank charges during 2004-5 was slightly lower than for the same period last year due to lower outstanding balances on operating lines. Interest on long-term debt for the three months ended June 30, 2005 was up slightly million compared to the same period in 2003-4 due to the slightly higher interest rates and principal amount outstanding compared to those in the same period in 2003-4.

Interest on margin loans for investment in marketable securities increased 174% to $0.62 million for 2004-5 or 135% to $0.19 million for the quarter ended June 30, 2005. The increase is due to a comparable increase in margin loan balances. The margin loans incurred an average interest rate of approximately 5% on the simple average margin loan balance outstanding during 2004-5.

### Other Income

For the 2004-5 year, the Corporation's realized gains and distribution income from portfolio investments generated $3.1 million of other income after margin loan interest costs compared to $1.7 million for 2003-4. Just over half of this year's realized gains and distribution income were generated in second quarter of 2004-5. Each of the remaining quarters also contributed positively to such increase and exceeded the investment income achieved by the Corporation's portfolio in the same quarter in 2003-4 except for the last quarter where the three months ended June 30, 2004 generated slightly higher net investment income. During the fourth quarter the Corporation realized gains and distribution income from portfolio investments of $0.34 million after margin loan interest costs compared to $0.6 million for the same period in 2003-4.

While the Corporation's distribution income is somewhat more predictable, the amount and timing of realized investment gains from the Corporation's marketable securities portfolio fluctuates materially from period to period subject to numerous factors beyond the Corporation's control including overall stock and capital market movement.

The Corporation recorded $0.65 million as its proportionate share of income for 2004-5 from its equity investment in Somerset Properties Ltd. This represented an over 300% increase compared to the equity income recorded from Somerset in 2003-4. Somerset's income was generated from realized gains and distribution income on its marketable securities portfolio as well as a realized gain on the sale of its office building during the first quarter.

### Corporate and administrative expenses

Recorded corporate and administrative expenses increased 10% to $1.4 million in 2004-5. This increase was due to the legal and financing costs related to the new loans secured by the Corporation during the fiscal year and the additional personnel hired at the beginning of the year for the investment division, offset in part by the lower actual audit expenses incurred by the Corporation compared to 2003-4. Corporate and administrative expenses for the fourth quarter of 2004-5 were $0.5 million, up by 17% for the same reasons as the year over year analysis.

### Net income before and after income taxes

Net income before and after income taxes increased 94% and 86% to $4.0 million and $3.3 million, respectively for 2004-5 compared to the prior fiscal year. These large increases were primarily due to:

- Realized gains and income on the Corporation's marketable securities portfolio.
- Proportionate income from Somerset Properties Ltd.

For the three months ended June 30, 2005, net income before and after income taxes declined 15% and 106% to $0.09 million and a net loss of $0.01 million, respectively. These decreases compared to 2003-4 were due to the lower operating income realized in the Food Division as well as greater realized investment gains in the fourth quarter of 2003-4 compared to 2004-5.

Tax expense for 2004-5 increased 148% to $0.7 million, $0.43 million (59%) of which is expected to be current taxes. This increase was less than the corresponding increase in net income due to the current large portion of the Corporation's income being derived from its marketable securities portfolio and different deductions being available to the Corporation for that income in contrast to its operating income from the Food Division. Future taxes in 2004-5 increased due to the timing differences relating to the depreciation of additional equipment acquired during the year.

### Funds from operations, EBITDA

Funds from operations for 2004-5 decreased materially by 9% to $2.1 million compared to 2003-4. This was mainly due to the reduced operating margin in the Frozen Food Unit and to a lesser extent the Bakery Unit as well as the fact that a substantial portion of net income is derived from the Corporation's investment activities and from its equity investment in Somerset Properties Ltd. These negative factors were partially offset by the termination of the $90,000 per quarter royalty previously owing by the Corporation in respect of certain products sold by the Frozen Food unit.

Funds from operations for the quarter ended June 30, 2005 increased materially by 161% to $0.3 million compared to the same period in 2003-4. This increase is due to the larger operating margin achieved by the Food Unit due to the stronger sales as well as the greater amount of distribution income received by the Corporation in the fourth quarter of 2004-5.

EBITDA for 2004-5 increased 46% to $7.2 million ($0.41 per share) compared to $4.9 million ($0.28 per share) in the prior year, again principally due to stronger investment income and gains. EBITDA for the three months ended June 30, 2005 increased 16% to $1.0 million ($0.06 per share) compared to $0.8 million ($0.05 per share) for the same period in the prior year, principally due to the smaller operating loss.

The material difference between EBITDA and funds flow is due to the fact that all realized gains in the Investment Division are reinvested into the marketable securities portfolio and together with the income from Somerset Properties Ltd., which is 40% owned by the Corporation are therefore not available for other financing activities of the Corporation. This is partly offset in the funds flow calculation with the exclusion of depreciation and amortization as well as future taxes.

### Working Capital

Cash and term deposits were down slightly (2%) compared to those at the beginning of the 2004-5 fiscal year, though the working capital ratio remained the same as at the beginning of the year at 1.29 times. If marketable securities and margin loans are excluded from working capital, the remaining working capital declined by $0.5 million producing a working capital ratio of 0.96 times.

Accounts receivable were materially lowered by 18% compared to the fiscal year opening balances due to improved collection practices especially in the Bakery Unit. Inventories decreased slightly during the fourth quarter of 2004-5 to result in an overall decline of $0.13 million or 4% compared to the level outstanding at the beginning of the fiscal year principally due to reductions in inventories in the Frozen Food Unit, partially offset by an increase in inventories in the Bakery Unit.

Prepaid expenses increased by $0.13 million or 76% due to deposits paid by the Bakery Unit for transportation and other equipment under various leases.

### Investing activities

Approximately $1.7 million of capital expenditures were incurred in 2004-5 being approximately the same total as in 2003-4. $0.3 million of these funds were expended for the purchase of First Gourmet Foods, an additional $0.2 million on equipment to allow First Gourmet Foods to produce a product line sold by the Bakery Unit in other markets with the balance on equipment and product development research for both the Bakery Unit and the Frozen Food Unit. $0.4 million of the total capital expenditures were applied to product research and development, packaging and product design and other intangible items. Approximately $0.5 million of capital expenditures were incurred in the fourth quarter of 2004-5 again comparable to amount in the same quarter of 2003-4.

### Financing Activities

*Loans*

During 2004-5 the Corporation decreased its bank loans by $0.26 million compared to the balance at the beginning of the year. During the fourth quarter of 2004-5 the Corporation increased its bank loans by $0.3 million compared to the balance at the beginning of the quarter due to normal operations.

During the 2004-5 year, the Corporation secured two new facilities for an aggregate of $1.9 million (described in "Liquidity and Capital Resources"). After normal principal payments and the use of $0.6 million of those proceeds to refinance other bank and long term debt, total long term debt only increased by $0.6 million or 6% compared to the fiscal year opening balance. The new facilities helped reduce the current portion of long term debt by 16% or $0.23 million compared to the current portion at the beginning of the year.

Margin loans incurred for investment in marketable securities increased 177% to $18.0 million from the amount outstanding at the beginning of the fiscal year. The outstanding margin loan balance at June 30, 2005 represented 70% of the Corporation's book value of its marketable securities (or 60% of its then market value). The margin loan balance at June 30, 2004 was 63% of the book value of its marketable securities (or 59% of its then market value).

*Repurchase of Common shares*

In June 2004, the Corporation received approval from The TSX Venture Exchange to acquire an additional 887,179 shares, representing approximately 5% of the issued and outstanding class "A" shares, through a seventh Normal Course Issuer Bid. During 2004-5, the Corporation repurchased approximately 458,000 shares from the market for an aggregate cost of $0.4 million (or an average of $0.96 per share) in a continued effort to improve shareholder value. During the fourth quarter of 2004-5, the Corporation repurchased approximately 87,000 shares from the market for an aggregate cost of $0.07 million (or an average of $0.85 per share).

### Related Party Transactions

The following related party transactions occurred during the fourth quarter of 2004-5.

The Corporation paid interest on convertible debentures and promissory notes due to shareholders of the Corporation in respect of advances made prior to the commencement of this fiscal year. The principal of these loans consist of the following: A) a $100,000 convertible debenture due to a shareholder and former officer of the Corporation, unsecured, bearing interest at 10% per annum compounded annually and payable on a monthly basis, with the principal portion repayable in full on July 1, 2007. The debenture is convertible at any time up to maturity, at the option of the holder, into 166,667 Class A common shares. These funds were originally used for working capital; B) a $250,000 advance bearing interest at 13% maturing July 31, 2005 (which was recently extended to July 31, 2007 at the same interest rate), which funds were originally used to assist with the purchase of the First City Gourmet Foods assets.

The Corporation paid interest on $76,000 principal amount of promissory notes due to a shareholder and officer of the Corporation in respect of advances made prior to the commencement of this fiscal year. Approximately one quarter of these advances bears interest ranging from 5 to 10% per annum and the balance bears interest at 10% to 12% per annum. The notes are unsecured and with no fixed terms of repayment. The original advances were an addition to working capital.

Management fees were charged by companies associated with the Chairman and CEO and Vice Chairman of the Corporation for management services which are included in corporate and administrative expenses aggregating $293,000 during the quarter.

Fees were paid to current and former directors of the Corporation for professional, management and other services rendered during the quarter in the ordinary course of business. The aggregate $296,000 of such expenses were included in corporate and administrative expenses ($241,000) and operating expenses ($55,000) during the quarter.

The above transactions also occurred through the first nine months of 2004-5. In addition, the following related party transactions occurred during the first nine months of 2004-5 only. During the third quarter, the Corporation advanced $144,000 to Somerset Properties Ltd. Those funds together with funds from a proportionate advance by Somerset's other shareholders were used by Somerset to purchase 600,000 Beaumont common shares for a total purchase price of $360,000 from a company controlled by the Corporation's Vice Chairman. Somerset also agreed to purchase from the same company an additional 600,000 Beaumont common shares in annual instalments over the following eight years at a purchase price of $1.10 per share plus 25% of the difference between the respective year end market price and $1.10. The average purchase price of the 1.2 million shares using the base price is $0.85 per share.

## Liquidity and Capital Resources

During 2004-5, the Corporation through its subsidiaries secured new loan facilities for an aggregate of $1.9 million. $1.0 million was secured through second mortgages on the Corporation's Calgary buildings, the proceeds of which were used for investment in the Corporation's investment portfolio ($0.7 million) and for working capital ($0.3 million). The second mortgage loans each have a term of two years, bear interest at 14.5% and the principal less minor amortization payments is due at maturity.

The remaining $0.9 million loan facility obtained during the quarter was secured by the Bakery Unit and was used to refinance previous equipment purchases ($0.6 million) and for new equipment purchases ($0.3). This loan facility bears interest at 0.25% above the lender's variable personal property loan rate (an initial interest rate of 5.75% at the time of advance), with principal payments amortized over the seven year term of the loan facility. In addition to general security provided by the Corporation, Winston Ho Fatt was also required to provide a capital call agreement as additional security.

Principal repayments, the above financings and the growth in the Corporation's equity resulted in a reduction of the long term debt to equity ratio to 0.79:1 at June 30, 2005 from 0.95:1 at June 30, 2004. The ratio of total liabilities to equity for the same dates however increased to 2.53:1 from 2.12:1 due these same factors combined with the increase in margin loans.

At June 30, 2005, the Corporation had total operating credit facilities of $3.6 million with various institutions, of which $2.4 million had been drawn down, and a balance of $1.2 million remained available. The operating facilities may be drawn down or repaid at any time, and there are no scheduled repayment terms. The Corporation believes that available cash flow from operations, working capital surplus and its borrowing facilities will be sufficient to fund these capital expenditures and debt repayment obligations. The Corporation and its affiliates were in compliance with all banking ratios during the fourth quarter except Mrs. Willman's which had exceeded the limit on capital expenditures. This event has since been waived as a default by the relevant lender.

### Summary of quarterly results

$ millions (except per share data)

| | 2005 | | | | | 2004 | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Q1 | Q2 | Q3 | Q4 | Total | Q1 | Q2 | Q3 | Q4 | Total |
| Revenues | $10,344 | $11,653 | $9,203 | $8,976 | $40,141 | $9,673 | $11,298 | $9,425 | $7,179 | $37,575 |
| Net income (loss) | 1,329 | 1,577 | 421 | (12) | 3,314 | 605 | 598 | 379 | 201 | 1,783 |
| Earnings (loss) per share | 0.00 | 0.03 | 0.09 | 0.07 | 0.19 | 0.03 | 0.03 | 0.02 | 0.02 | 0.10 |

2005 quarterly revenues followed historical seasonal trends with the first half of the year, especially the second quarter posting the strongest sales results. 2005 quarterly net income results were affected by realized gains on the investment portfolio as well as seasonal operating results from the Food Division.

## DIVISIONAL REPORTING

### Food Processing Division

The strong Canadian dollar, warm weather during the Frozen Food Unit's historically strongest quarter and historically high ingredient, packaging and transportation costs adversely affected sales and operating margins during 2004-5. This was partially offset in the Bakery Unit through commencement of new product lines. The Frozen Food Unit continues to pursue new product lines to differentiate its products. These activities are expected to offset part of declines expected in historical product lines and the effect of the continuing strong Canadian dollar as well as historically high ingredient, packaging, transportation and energy costs. The Bakery Unit also looks to introduce new products or differentiate historical products as it faces similar issues such as the effect of the strong Canadian dollar and historically high ingredient, packaging, transportation and energy costs.

While the Food Processing Division continues to research new product opportunities, more of the near term growth is anticipated to come from acquisitions and consolidation in the baked goods area.

### Investment Division

During the fourth quarter the investment portfolio achieved more modest returns relative to the returns experienced during the first three quarters of 2004-5, with the net return after margin loan interest during the quarter being approximately $0.3 million.

During the 2004-5 fiscal year, the marketable securities portfolio achieved an investment return of approximately 10%, measured against the total capital employed as of June 30, 2005 ($29.9 million). This return on capital figure is based on realized capital gains on investments and distributions received on investments and income trust units held, less interest paid on margin loans. Including unrealized gains in such a calculation would increase the return on capital employed to 23%. Margin loans of $18.0 million at June 30, 2005 comprised approximately 60% of such total capital. Realized gains ($2.6 million) and distribution income ($1.1 million) for 2004-5 represented a 62% return on equity, based on the July 1, 2004 opening equity balance in the portfolio plus capital additions to the portfolio from the Corporation's other funding sources. Unrealized gains at the end of the fourth quarter for the Corporation were in excess of $3.7 million.

At June 30, 2005, the marketable securities portfolio was comprised of investments in a wide range of businesses, with the substantial majority of the overall capital concentrated in the energy sector. At the end of the quarter approximately 62% of the total market value of the portfolio was invested in oil and gas exploration and development companies and energy trusts with an additional 11% invested in energy services businesses. During the fourth quarter, continuing increases in the value of the Corporation's investments in this sector prompted a deferral of a planned shift of part of that portfolio to other business sectors. In keeping with the Corporation's investment strategy, approximately 58% of the total market value of the portfolio was comprised of income or energy trusts with regular cash distributions. Towards the end of the third quarter, the Corporation invested an additional $700,000 into its portfolio from loan proceeds obtained by the Corporation through a second mortgage over its Calgary properties.

At the end of the fourth quarter, the four largest investments comprised approximately 42% of the total portfolio's market value. All of these investments were in the oil and gas sector three of which are energy trusts each with a market capitalization in excess of $750 million and the fourth a junior oil and gas company with a market capitalization in excess of $500 million. The balance of the portfolio included investments in approximately 70 different companies, one third of which companies are investments of less than $100,000 individually or $1.0 million in the aggregate.

The Corporation will continue to monitor the prospects for positive returns from it energy sector investments while gradually reducing the amount of margin capital employed. In the medium term, the Corporation will continue to the diversification of the portfolio across various market sectors and types of investments.

The Corporation is affiliated with Somerset Properties Ltd., in which the Corporation holds a 40% interest. Associates of the Corporation's Chairman and CEO own the remaining 60%. Somerset is involved in investing in a marketable securities portfolio, as well as real estate. The Somerset investment strategy is somewhat more aggressive than the Corporation's in terms of capital risk and leverage employed. However, the portfolios of both companies contain mostly common securities.

As of June 30, 2005, Somerset's marketable securities portfolio employed approximately $14.6 million of capital, of which margin loans represented approximately 61%. During the 2004-5 Somerset achieved a return on capital of 12%, measured against the total capital employed as of June 30, 2005. This return on capital figure is based on realized capital gains on investments and distributions received on investment and income trust units held, less interest paid on margin loans. Including unrealized gains in such a calculation would increase the return on capital employed to 26%. Realized gains and distribution income for 2004-5 represented a 91% return on Somerset's equity, based on the July 1, 2004 opening equity balance of the portfolio plus capital additions since then. Unrealized gains at the end of 2004-5 were in excess of $2.1 million.

### Real Estate Division

During 2004-5 this division assisted other divisions through securing of financing. In the third quarter, the Realty division secured an aggregate of $1 million of second mortgage loans against its Calgary properties which were ultimately advanced to affiliates. Otherwise, no material changes in this division's activity occurred during 2004-5.

Somerset's subsidiary Talisman Homes Ltd. was able to reverse prior losses during the first nine months to realize a small profit during 2004-5. Somerset also completed the sale of its office building during the first quarter generating a gain of $0.6 million. Recent activity in the vicinity of Somerset's 91 acre property situate west of Calgary suggests that the value of same has more than doubled since Somerset's acquisition thereof for $0.9 million in June 2003.

## CORPORATE

Pursuant to new disclosure rules applicable to the Corporation, the chief executive officer and chief financial officer of the Corporation (in this case Winston Ho Fatt, who fills both roles) are required to evaluate the effectiveness of the Corporation's disclosure controls and procedures as of the end of June 30, 2005 and to disclose those conclusions in this MD&A.

The Corporation has a very flat management structure which already has adequate procedures for the prompt identification to the Chairman and CEO and other senior management of the Corporation of material or potentially material facts and developments regarding all aspects of the business of the Corporation, its subsidiaries and associated companies. The Corporation's senior management is familiar with the disclosure obligations of public companies like the Corporation. In addition, senior management personnel regularly consult with the Corporation's legal and accounting advisors regarding changes in applicable rules and regulations regarding disclosure as well as matters of judgment in the application of those rules and regulations to the Corporation's affairs.

Based on this framework, the Corporation's Chairman and CEO has determined that the current controls and other procedures of the Corporation are designed to provide reasonable assurance that information required to be disclosed by the Corporation in its annual filings, interim filings or other reports filed or submitted by it under securities legislation is recorded, processed, summarized and reported within the time periods specified in the securities legislation. Also the Corporation's controls and procedures are designed to ensure that information required to be disclosed by an issuer in its annual filings, interim filings or other reports filed or submitted under securities legislation is accumulated and communicated to the issuer's management, including its chief executive officer and chief financial officer, as appropriate to allow timely decisions regarding required disclosure.

## OUTLOOK

In light of the Canadian dollar moving to levels not recently experienced and the uncertainty regarding the impact of high energy costs on consumer demand and most input costs including ingredient costs and transportation costs for the balance of 2005-6, the Corporation is unable to provide any specific guidance on anticipated operating income, funds flow from operations and EBITDA for 2005-6. The Investment Division results are again not predictable for 2005-6. Since July 1, 2005 though, investment returns from the marketable securities portfolio and from the Corporation's share of income from Somerset Properties Ltd. have continued to provide additional contribution to EBITDA and net income. At September 30, 2005, the total capital employed in the portfolio has increased to over $42 million and realized and unrealized gains have in aggregate exceeded $4 million.

## FORWARD LOOKING STATEMENTS

This annual report may contain forward-looking statements including statements regarding the business and anticipated financial performance of the Corporation. These forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results and performance of the Corporation to be materially different from the future results and performance expressed or implied by such forward-looking statements. A number of factors could affect the actual results, including but not limited to, input costs, competition, and access to capital market. In light of the significant uncertainties inherent in the forward-looking statements, the inclusion of such information should not be regarded as a representation by the Corporation that the objectives and plans of the Corporation will be achieved. The Corporation will not necessarily update the forward-looking statements as information becomes available.

## ADDITIONAL INFORMATION

For additional information on the Corporation, readers should also refer to the information filed on www.sedar.com.

## A NOTE OF THANKS

We wish to take this opportunity to thank all of our managers, supervisors and employees who, as associates, worked so hard to make this another successful year.

Winston Ho Fatt
Chairman and Chief Executive Officer

## MANAGEMENT'S RESPONSIBILITY FOR FINANCIAL STATEMENTS

The accompanying consolidated financial statements of Beaumont Select Corporations Inc. have been prepared by management in accordance with Canadian generally accepted accounting principles consistently applied. The Corporation's accounting procedures and related systems of internal control are designed to provide reasonable assurance that its assets are safeguarded and its financial records are reliable. In recognizing that the Corporation is responsible for both the integrity and objectivity of the financial statements, management is satisfied that these financial statements have been prepared with this in mind and within the information presented in the financial statements.

Meyers Norris Penny LLP (MNP), Chartered Accountants, who were appointed by the shareholders of the Corporation at its annual meeting on December 15, 2004 to serve as the Corporation's external auditors until the next annual meeting of shareholders, have examined the consolidated financial statements of the Corporation for the year ended June 30, 2005 and 2004.

The Audit Committee has reviewed these statements with management and the auditors, and has reported to the Board of Directors. The Board has approved the consolidated financial statements of the Corporation herein.

Winston Ho Fatt
Chairman and Chief Executive Officer

## AUDITORS' REPORT TO THE SHAREHOLDERS

We have audited the consolidated balance sheets of Beaumont Select Corporations Inc. as at June 30, 2005 and 2004 and the consolidated statements of operations and retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Corporation's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Corporation as at June 30, 2005 and 2004 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Meyers Norris Penny LLP
Chartered Accountants

Calgary, Canada
September 28, 2005

# Consolidated Balance Sheets

*June 30, 2005 and 2004 (in thousands of dollars)*

| | 2005 | 2004 |
|---|---|---|
| **ASSETS** | | |
| Current assets: | | |
| Cash | **$ 1,045** | $ 1,067 |
| Marketable securities (note 2) | **25,669** | 10,324 |
| Accounts receivable | **2,445** | 2,983 |
| Inventory (note 3) | **3,513** | 3,642 |
| Prepaid expenses | **312** | 177 |
| Current portion of loans receivable (note 4) | **55** | 78 |
| | **33,039** | 18,271 |
| Loans receivable (note 4) | **75** | 74 |
| Investment in and due from affiliated company (note 5) | **1,707** | 979 |
| Property and equipment (note 7) | **15,276** | 15,421 |
| Goodwill | **926** | 926 |
| Intangible assets (note 8) | **1,086** | 944 |
| Future income tax assets (note 12) | **569** | 771 |
| | **$ 52,678** | $ 37,386 |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | |
| Current liabilities: | | |
| Bank loans (note 9) | **$ 2,363** | $ 2,617 |
| Accounts payable and other liabilities | **3,809** | 3,635 |
| Margin loans on marketable securities investment (note 2) | **18,026** | 6,497 |
| Current portion of long-term debt (note 9) | **1,474** | 1,440 |
| | **25,672** | 14,189 |
| Related party transactions (note 6) | **352** | 235 |
| Future income taxes (note 12) | **1,533** | 1,440 |
| Long-term debt (note 9) | **10,373** | 9,776 |
| Shareholders' equity: | | |
| Share capital (note 10) | **8,231** | 8,325 |
| Contributed surplus (note 11) | **4** | – |
| Retained earnings | **6,513** | 3,421 |
| | **14,748** | 11,746 |
| Commitment (note 15) | | |
| Subsequent events (note 17) | | |
| | **$ 52,678** | $ 37,386 |

*See accompanying notes to consolidated financial statements.*

On behalf of the Board:

Winston Ho Fatt
Director

Peter Kreutzer
Director

# Consolidated Statements of Operations and Retained Earnings

*Years ended June 30, 2005 and 2004 (in thousands of dollars except per share information)*

| | 2005 | 2004 |
|---|---|---|
| Revenues (note 14) | **$ 39,741** | $ 37,575 |
| Cost of sales: | | |
| Direct expenses | **35,471** | 32,940 |
| Depreciation and amortization | **1,441** | 1,452 |
| | **36,912** | 34,392 |
| Operating margin | **2,829** | 3,183 |
| Operating expenses: | | |
| Corporate and administrative (note 6) | **1,406** | 1,281 |
| Interest on long-term debt | **727** | 725 |
| Short-term interest and bank charges | **105** | 111 |
| Royalty (note 6) | **–** | 360 |
| Depreciation and amortization | **298** | 321 |
| | **2,536** | 2,798 |
| Income before the following | **293** | 385 |
| Other income (expenses): | | |
| Write-down of marketable security (note 2) | **–** | (92) |
| Interest on margin loans (note 2) | **(617)** | (225) |
| Investment income (note 2) | **1,147** | 464 |
| Gain on sale of marketable securities | **2,570** | 1,416 |
| Income from affiliated company (note 5) | **651** | 151 |
| Stock-based compensation (note 11) | **(4)** | – |
| Foreign exchange gain | **–** | 16 |
| Write-down of intangible assets (note 8) | **–** | (39) |
| | **3,747** | 1,691 |
| Income before income taxes | **4,040** | 2,076 |
| Income taxes (note 12): | | |
| Current | **430** | 70 |
| Future | **296** | 223 |
| | **726** | 293 |
| Net income | **3,314** | 1,783 |
| Retained earnings, beginning of year | **3,421** | 2,353 |
| Excess of consideration paid over stated value of shared redeemed (note 10) | **(222)** | (219) |
| Dividends paid on common shares | **–** | (496) |
| Retained earnings, end of year | **$ 6,513** | $ 3.421 |
| Net income per share (note 10): | | |
| Basic | **$ 0.19** | $ 0.10 |
| Diluted | **$ 0.19** | $ 0.10 |

*See accompanying notes to consolidated financial statements.x*

# Consolidated Statements of Cash Flows

*Years ended June 30, 2005 and 2004 (in thousands of dollars)*

| | 2005 | 2004 |
|---|---|---|
| Cash provided by (used in): | | |
| Operations: | | |
| Net income | **$ 3,314** | $ 1,783 |
| Add (deduct) items not requiring cash: | | |
| Depreciation and amortization | **1,739** | 1,773 |
| Write-down of marketable security | **–** | 92 |
| Future income taxes | **296** | 223 |
| Gain on disposal of marketable securities | **(2,570)** | (1,416) |
| Income from affiliated company (note 5) | **(650)** | (151) |
| Expenses recognized on stock-based compensation (note 11) | **4** | – |
| Write-down of intangible assets | **–** | 39 |
| Funds from operations | **2,133** | 2,343 |
| Net change in non-cash working capital balances (note 16) | **(543)** | (1,631) |
| | **1,590** | 712 |
| Investing: | | |
| Purchase of property and equipment | **(1,296)** | (1,198) |
| Expenditures on intangible assets | **(439)** | (500) |
| Increase in loans receivable | **(54)** | (342) |
| | **(1,789)** | (2,040) |
| Financing: | | |
| Increase (decrease) in bank loans, net of repayments | **(254)** | 1,405 |
| Repurchase and cancellation of Class A common shares | **(438)** | (396) |
| Issue of Class A common shares | **121** | 93 |
| Dividends paid on common shares | **–** | (496) |
| Increase in long-term debt, net of repayments | **631** | 627 |
| Increase in due to related parties | **117** | 13 |
| | **177** | 1,246 |
| Decrease in cash during the year | **(22)** | (82) |
| Cash, beginning of year | **1,067** | 1,149 |
| Cash, end of year | **$ 1,045** | $ 1,067 |

*See accompanying notes to consolidated financial statements.*

# Notes to Consolidated Financial Statements

*Years ended June 30, 2005 and 2004*

**GENERAL:**

Beaumont Select Corporations Inc. (the "Corporation") is incorporated under the Business Corporations Act of Alberta. The Corporation's primary operations relate to food processing and distribution, real estate and investments.

## 1. SIGNIFICANT ACCOUNTING POLICIES:

The consolidated financial statements of the Corporation have been prepared in accordance with Canadian generally accepted accounting principles. In the preparation of these consolidated financial statements, management has made estimates and assumptions that affect the recorded amounts of certain of the Corporation's assets, liabilities, revenues and expenses and the disclosure of contingent assets and liabilities. The most significant estimate relates to determining the cost recoverability of the Corporation's goodwill and other intangible assets, which are principally based upon estimated future cash flows. While it is the opinion of management that these consolidated financial statements have been properly prepared within reasonable limits of materiality and within the framework of the significant accounting policies summarized below, actual results could differ from the estimates made.

***(a) Basis of presentation:***

The consolidated financial statements include the accounts of the Corporation and its subsidiaries. Certain of the comparative figures have been reclassified to conform to the current year's financial statement presentation.

***(b) Inventory:***

Inventory is recorded at the lower of cost (first in, first out basis) and market, with market determined at net realizable value.

***(c) Property and equipment:***

Property and equipment are recorded at cost upon acquisition. Depreciation on property and equipment is provided using principally the straight-line method over the estimated useful lives of the assets as follows:

| Asset | Estimated Useful Life |
|---|---|
| Production equipment | 10 to 20 years |
| Buildings | 10 to 20 years |
| Leasehold improvements | 10 years |
| Vehicles | 6 to 10 years |

***(d) Goodwill and other intangibles:***

Goodwill represents the excess of cost over the fair value of net assets acquired. Other intangible assets relate to deferred financing costs associated with the refinancing of long-term debt and deferred development costs associated with the development of new commercially viable product lines and packaging designs. Management tests goodwill and other intangible assets for impairment at the end of the Corporation's fiscal year, taking into consideration the nature of the industry and the circumstances which might impair the value. The amount of impairment, if any, is determined based on estimated future cash flows. Any impairment in the value of the goodwill or other intangibles is charged in the period when impairment is determined. Other intangibles relating to deferred development costs are amortized on a straight-line basis over periods ranging from five to ten years and deferred financing costs are amortized over the term of the corresponding debt facility.

***(e) Asset retirement obligations:***

Asset Retirement Obligations are measurements of liabilities related to legal obligations associated with the retirement of property, plant and equipment. The fair value of the asset retirement obligations are to be recorded and capitalized on a discounted basis as part of the cost of the related asset, and amortized to expense over its useful life.

## 1. SIGNIFICANT ACCOUNTING POLICIES: *continued*

### *(f) Foreign currency translation:*

Integrated foreign operations have been translated into Canadian dollars using the temporal method as follows:

Monetary items – exchange rates in effect at the balance sheet date;

Non-monetary items – exchange rates in effect on the dates of those transactions; and

Revenues and expenses – at the average exchange rate prevailing during the year; except for depreciation and amortization, which is translated at prevailing rates when the respective assets were acquired. Gains and losses arising from the translation are included in income for the current year.

### *(g) Marketable securities:*

Marketable securities are stated at the lower of cost and market value.

### *(h) Per share amounts:*

Basic net income per share is calculated using the weighted average number of common shares outstanding during the year. Diluted net income per share is calculated following the treasury stock method assuming that the proceeds obtained upon the exercise of options would be used to purchase common shares at the average market price during the period.

### *(i) Income taxes:*

The Corporation follows the liability method of accounting for income taxes. Under this method, future income tax liabilities and future income tax assets are recorded based on temporary differences – the difference between the carrying amount of an asset and liability in the consolidated balance sheet and its tax basis using income tax rates enacted at the balance sheet date. The effect of changes in rates on future income tax liabilities and assets is recognized in the period that the change occurs.

### *(j) Stock-based compensation:*

In accordance with the Corporation's stock option plan, common share options may be granted to directors, officers, consultants and certain employees. In determining the stock-based compensation, the Corporation applies the Black-Scholes valuation method, and records same as expense over the vesting period for stock options granted to the option holders. When stock options are exercised for common shares, consideration paid by the option holders and the previously recognized liability associated with the stock options are recorded as share capital. Accrued compensation for forfeited stock options is adjusted to earnings by decreasing the compensation liability in the period of occurrence. No compensation expense has been recorded for awards granted prior to 2003.

### *(k) Long-term investment:*

The Corporation's long-term investment represents a 40% ownership interest in Somerset Properties Ltd. ("Somerset") (see note 5) and is accounted for using the equity method. Under this method, the investment account was recorded at its carrying value on June 30, 2003, the date in which the Corporation sold 60% of its ownership interest in Somerset, and is adjusted by the Corporation's proportionate share of Somerset's net earnings or losses and dividends received. The carrying value of the long-term investment is periodically reviewed by management to determine if the facts and circumstances suggest that it may be permanently impaired. Any impairment identified through this assessment would result in a write-down of the investment and a corresponding charge to income.

### *(l) Revenue recognition:*

Revenue from product sales are net of returns and credit notes and are recorded when delivery has been made and legal ownership of the product has been transferred to the customer.

## 2. MARKETABLE SECURITIES:

At June 30, 2005, the Corporation held marketable securities with a fair market value of $29.9 million (2004 – $10.8 million) of which $18.7 million, or 73% was in the oil and gas industry (2004 – $6.8 million or 63%). The top three holdings of the investment portfolio were also in the oil and gas industry with a fair market value of $11.5 million or 38% (2004 – $4.1 million, or 38%). In addition, the Corporation has margin loans totaling $18.0 million (2004 – $6.5 million). Marketable securities are held as collateral to satisfy the requirements of the margin loans.

## 3. INVENTORY:

| | 2005 | 2004 |
|---|---|---|
| Raw materials | $ 2,344 | $ 2,465 |
| Finished goods | 1,169 | 1,177 |
| | $ 3,513 | $ 3,642 |

## 4. LOANS RECEIVABLE:

| | 2005 | 2004 |
|---|---|---|
| Non-interest bearing loans receivable of which $70,000 is secured by a second charge on all of the assets of the debtor. The remaining balance is unsecured with varying repayment terms | $ 130 | $ 152 |
| Less current portion | 55 | 78 |
| | $ 75 | $ 74 |

## 5. INVESTMENT IN AND DUE FROM AFFILIATED COMPANY:

Investment in and due from affiliated Company consists of the Company's 40% investment in Somerset as well as advances due from Somerset. The Chairman and Chief Executive Officer of the Corporation owns, directly and indirectly, the remaining 60% of Somerset.

Somerset's primary operations relate to investing in a marketable securities portfolio which includes the use of margin loans. In addition, Somerset invests in real estate and is involved in the construction of homes in Calgary through a 52% ownership interest in Talisman Homes of Calgary.

Somerset's income and financial position are subject to stock and real estate market fluctuations.

During the year, Somerset acquired 600,000 Beaumont common shares for a total purchase price of $360,000 from a company controlled by the Corporation's Vice Chairman. Somerset has also agreed with the same company to acquire by 2012 an additional 600,000 Beaumont common shares at a price of $1.10 per share, plus 25% of the excess if any by which the market value of the Corporation's common shares exceed $1.10 prior to the time of purchase.

Details of the amount due from and investment in Somerset are as follows:

| | 2005 | 2004 |
|---|---|---|
| Investment in Somerset – beginning | $ 579 | $ 428 |
| Income from equity investment | 651 | $ 151 |
| Investment in Somerset – ending | 1,230 | 579 |
| Due from Somerset, unsecured, non-interest bearning, with no specific terms of repayment | 277 | 200 |
| Due from Somerset, unsecured, bearing interest @ 6% per annum, with no specific terms of repayment | 200 | 200 |
| Due from Somerset – ending | 477 | 400 |
| | $ 1,707 | $ 979 |

## 6. RELATED PARTY TRANSACTIONS:

### (a) Balance Sheet:

| | 2005 | 2004 |
|---|---|---|
| Convertible debenture due to a shareholder and former officer of the Corporation, unsecured, bearing interest at 10% per annum compounded annually and payable on a monthly basis, with the principal portion repayable in full on July 1, 2007. The debenture is convertible at any time up to maturity, at the option of the holder, into 166,667 Class A common shares ............ | $ 100 | $ 100 |
| Promissory note due to a shareholder and former officer of the Corporation, unsecured, bearing interest at 13% per annum, interest to be paid monthly, with the principal portion repayable in full on July 31, 2005. ............................... | 250 | – |
| Promissory notes due to shareholders of the Corporation, bears interest at 10% to 12% per annum. The notes are unsecured and with no fixed terms of repayment ................... | 76 | 135 |
| A loan agreement with an officer and director of the Corporation whereby the Corporation loaned the officer $69,362, secured with collateral, payable on demand, bearing interest at 7% per annum and to be accrued annually, maturing on June 30, 2007......... | (74) | – |
| | $ 352 | $ 235 |

### (b) Income statement:

| | 2005 | 2004 |
|---|---|---|
| (i) Royalty charged by a company in which the chairman of the Corporation is the president but not a shareholder..................... | $ – | $ 360 |
| (ii) Management fees charged by shareholders of the Corporation included in corporate and administrative expenses..................... | $ 677 | $ 766 |
| (iii) Interest revenue on amounts due from an officer and shareholder of the Corporation included in revenues ................... | $ 5 | $ 5 |
| (iv) Interest expense on amounts due to shareholders of the Corporation ........................................ | $ 51 | $ 12 |
| (v) Consulting fees paid to a shareholders, current and former officers of the Corporation, included in corporate and administrative expenses ........................... | $ 241 | $ 64 |

The transactions were conducted in the normal course of operations and measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

## 7. PROPERTY AND EQUIPMENT:

| 2005 | Cost | Accumulated depreciation | Net book value |
|---|---|---|---|
| Production equipment | $ 25,263 | $ 13,855 | $ 11,408 |
| Buildings | 3,459 | 1,743 | 1,716 |
| Leasehold improvements | 2,518 | 1,676 | 842 |
| Vehicles | 1,069 | 674 | 395 |
| Land | 915 | – | 915 |
| | $ 33,224 | $ 17,948 | $ 15,276 |

During the year, the Corporation purchased approximately $320,000 of manufacturing and baking equipment coupled with other related properties from an unrelated party.

| 2004 | | | |
|---|---|---|---|
| Production equipment | $ 24,289 | $ 12,808 | $ 11,481 |
| Buildings | 3,459 | 1,608 | 1,851 |
| Leasehold improvements | 2,413 | 1,440 | 973 |
| Vehicles | 852 | 651 | 201 |
| Land | 915 | – | 915 |
| | $ 31,928 | $ 16,507 | $ 15,421 |

## 8. INTANGIBLE ASSETS:

| 2005 | Cost | Accumulated depreciation | Net book value |
|---|---|---|---|
| Deferred development costs | $ 2,979 | $ 2,014 | $ 965 |
| Deferred finance costs | 391 | 270 | 121 |
| | $ 3,370 | $ 2,284 | $ 1,086 |

| 2003 | | | |
|---|---|---|---|
| Deferred development costs | $ 2,582 | $ 1,742 | $ 840 |
| Deferred finance costs | 349 | 245 | 104 |
| | $ 2,931 | $ 1,987 | $ 944 |

The Corporation recorded no write-down due to any permanent impairment in 2005 (2004 – $38,655).

## 9. BANK LOANS AND LONG-TERM DEBT:

### *(a) Bank loans:*

The bank loans are revolving lines of credit, repayable on demand, bearing interest at rates ranging from the bank's prime rate plus 0.5% to the bank's prime rate plus 1.25% per annum and are secured under various general security agreements covering, all present and after-acquired property of the Corporation, an assignment of life insurance on an officer and shareholder of the Corporation, a general assignment of accounts receivable and inventory, personal guarantees from an officer and shareholder of the Corporation and a postponement of claim by the Corporation.

### *(b) Long-term debt:*

| | **2005** | 2004 |
|---|---|---|
| Term loans, repayable in monthly principal instalments of approximately $92,000 plus interest ranging from the lenders' cost of funds to cost of funds plus 0.25% per annum, and the bank's prime rate plus 1.25% per annum, and secured as described in note 9(a) | **$ 6,647** | $ 6,793 |
| Mortgages, repayable in monthly principal instalments of approximately $26,000 bearing interest at rates ranging from the lenders' floating base rate to the lenders' cost of funds plus 2.75% per annum, and secured by the buildings (see note 7). Mortgages are not subject to renewal until dates ranging from November, 2008 to May, 2016 | **4,021** | 4,324 |
| Second mortgages, no principal repayment till the maturity on February 15, 2007, bearing interest rate at 15% per annum, paid monthly, with assignment of rents to lender | **1,016** | – |
| Capital leases, due 2005 through 2010, payable monthly, with interest rates ranging from 6.8% to 12% per annum and secured by certain equipment with a net book value at June 30, 2005 totaling approximately $212 thousand (2004 – $230 thousand) | **164** | 99 |
| | **11,847** | 11,216 |
| Less current portion | **1,474** | 1,440 |
| | **$10,373** | $ 9,776 |

Except as specifically disclosed, the Corporation has pledged as security for the various mortgages and loans, all of the assets of the Corporation.

The Corporation is required to make future principal payments as follows:

| | Long-term debt | Capital leases | Total |
|---|---|---|---|
| 2006 | $ 1,434 | $ 40 | $ 1,474 |
| 2007 | 2,471 | 34 | 2,505 |
| 2008 | 1,480 | 28 | 1,508 |
| 2009 | 2,709 | 25 | 2,734 |
| 2010 | 913 | 12 | 925 |
| Thereafter | 2,676 | 25 | 2,701 |
| | $ 11,683 | $ 164 | $ 11,847 |

## 10. SHARE CAPITAL:

*(a) Authorized:*

(i) Unlimited Class A voting common shares; and

(ii) 100,000,000 non-voting Class B shares, Series 2.

***(b) Class A common shares issued:***

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | **Shares** | **Amount** | Shares | Amount |
| Balance, beginning of year | **17,669,973** | **$ 8,325** | 17,866,473 | $ 8,410 |
| Redemption of shares | **(458,800)** | **(216)** | (376,500) | (177) |
| Issued for cash | **238,724** | **122** | 180,000 | 92 |
| Balance, end of year | **17,449,897** | **$ 8,231** | 17,669,973 | $ 8,325 |

During the year ended June 30, 2005 the Corporation acquired 458,800 (2004 – 376,500) Class A common shares for consideration consisting of cash proceeds totaling $438 thousand (2004 – $396 thousand). As the consideration rendered was in excess of the stated value of the shares, the amount in excess totaling $222 thousand, (2004 – $219 thousand) was recorded as a reduction of retained earnings.

***(c) Stock options:***

The Corporation has a stock option plan whereby officers, directors, employees and consultants may be granted options to purchase Class A common shares of the Corporation. As at June 30, 2005 options have been granted to purchase 440,000 (2004 – 603,724) Class A common shares at prices ranging from $0.53 to $0.94 until expiry on dates ranging from October 30, 2005 to March 1, 2010. Options vest at periods ranging from zero to four years and have a term of five years to expiry.

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | **Number** | **Weighted average exercise price** | Number | Weighted average exercise price |
| Outstanding options, beginning of year | **603,724** | **$ 0.52** | 783,724 | $ 0.52 |
| Granted | **180,000** | **0.94** | – | – |
| Exercised | **(238,724)** | **0.51** | (180,000) | 0.52 |
| Expired / cancelled | **(105,000)** | **0.50** | – | – |
| Outstanding options, end of year | **440,000** | **$ 0.70** | 603,724 | $ 0.52 |
| Options exercisable, end of year | **305,000** | **$ 0.59** | 583,724 | $ 0.52 |

| **Options Range of Exercise Price** | **Outstanding June 30, 2005** | **Weighted average remaining contractual life (years)** | **Exercisable June 30, 2005** | **Weighted Weighted average exercise price** |
|---|---|---|---|---|
| $0.53 | **260,000** | **0.33** | **260,000** | **$ 0.53** |
| $0.94 | **180,000** | **4.66** | **45,000** | **$ 0.94** |
| $0.53 to 0.94 | **440,000** | **2.10** | **305,000** | **$ 0.59** |

***(d) Per share amounts:***

The weighted average number of Class A common shares outstanding during the year ended June 30, 2005 was 17,571,065 (year ended June 30, 2004 – 17,768,655). The dilutive effect of options for the year ended June 30, 2005 was 283,509 (year ended June 30, 2004 – 448,632).

## 11. STOCK BASED COMPENSATION:

The Corporation has a stock option plan whereby officers, directors, employees and consultants may be granted the option to purchase Class A common shares of the Corporation.

For options granted prior to July 1, 2003, compensation expense has not been recognized and recorded in the income statement.

During the year ended June 30, 2005 the Corporation granted 180,000 options with a fair value of $0.34 per option, resulting in a charge of $4 thousand to current income and an increase of same to contributed surplus. The fair value of each option granted was determined using the Black-Scholes model with the following assumptions:

| | |
|---|---|
| Expected dividend yield | 0.0% |
| Risk free interest rate | 5.0% |
| Expected volatility | 30.0% |
| Expected life (in years) | 5.0 |

## 12. INCOME TAXES:

Total income taxes are different from the amount computed by applying the combined expected Canadian Federal and Provincial tax rate of 34.0% (2004 – 35.5%) to income before income taxes and other items. The reasons for the difference are as follows:

| | 2005 | 2004 |
|---|---|---|
| Computed expected tax provision | **$ 1,374** | $ 746 |
| Add (deduct) the tax effect of the following: | | |
| Impact of change in federal and provincial tax rates | **(61)** | (10) |
| Capital taxes | **58** | 17 |
| Change in valuation allowance | **(460)** | (223) |
| Non-taxable portion of capital gains | **(437)** | (262) |
| Non-taxable portion of write-down on marketable securities/receivables | **418** | 33 |
| Non-deductible expenses | **55** | 46 |
| Non-taxable from foreign and affiliated companies (note 5) | **(221)** | (54) |
| Total income taxes, as reported | **$ 726** | $ 293 |

The components of the net future income tax asset (liabilities) at June 30, 2005 and 2004 are as follows:

| | 2005 | 2004 |
|---|---|---|
| Future income tax liabilities: | | |
| Carrying value of property, equipment and intangible assets in excess of tax cost | **(1,533)** | (1,605) |
| Future income tax assets: | | |
| Non-capital losses | **$ 149** | $ 574 |
| Net capital and other losses | **3** | 132 |
| Tax cost of property, equipment and intangible assets in excess of carrying value | **417** | 690 |
| | **569** | 1,396 |
| Valuation allowance | **–** | (460) |
| Net future income tax liability | **$ (964)** | $ (669) |

At June 30, 2005 the Corporation had cumulative income tax deductions totaling approximately $13 million, including reported non-capital losses for income tax purposes of approximately $0.5 million which expire in the years 2007 to 2011.

Corporate tax returns are subject to assessment by taxation authorities in the normal course of business. The results of any assessments will be accounted for as a charge to earnings in the year in which they occur.

## 13. SEGMENTED INFORMATION:

Reportable segments are identified on the basis of internal reporting to senior management. The Corporation operates primarily through three operating groups being: 1) food processing and distribution, 2) real estate and rental properties, and 3) marketable securities investment. All operations are located in Canada.

Inter-segment eliminations relate to revenues between segments recorded at transfer prices based on current market prices. Operating margin represents total revenues less cost of sales, including depreciation. Operating expenses are comprised of interest, corporate, royalty, amortization and administrative charges. Identifiable assets by industry segment are the assets specifically attributable to those operations.

The following is an analysis of certain consolidated financial information by segment for the years ended June 30:

| | 2005 | 2004 |
|---|---|---|
| Revenues:(1) | | |
| Food processing and distribution | **$ 39,741** | $ 37,575 |
| Real estate and rental properties | **554** | 630 |
| Inter-segment transactions | **(554)** | (630) |
| | **$ 39,741** | $ 37,575 |
| Income before income taxes: | | |
| Food processing and distribution | **$ 792** | $ 847 |
| Real estate and rental properties | **(3)** | 92 |
| Inter-segment transactions | **(500)** | (576) |
| Marketable securities investment(2) | **3,751** | 1,713 |
| | **$ 4,040** | $ 2,076 |

(1) During the year ended June 30, 2005, sales totaling approximately $4.0 million (2004 – $4.8 million ) were made to customers located in the United States.

(2) Includes income from affiliated company (Note 5)

Property and equipment:

| **2005** | Food processing and distribution | Real estate and rental properties | Total |
|---|---|---|---|
| Production equipment | **$ 11,100** | **$ 308** | **$ 11,408** |
| Buildings | **–** | **1,716** | **1,716** |
| Leasehold improvements | **828** | **14** | **842** |
| Vehicles | **395** | **–** | **395** |
| Land | **–** | **915** | **915** |
| | **$ 12,323** | **$ 2,953** | **$ 15,276** |

| 2004 | Food processing and distribution | Real estate and rental properties | Total |
|---|---|---|---|
| Production equipment | $ 11,150 | $ 381 | $ 11,481 |
| Buildings | – | 1,851 | 1,851 |
| Leasehold improvements | 957 | 16 | 973 |
| Vehicles | 201 | – | 201 |
| Land | – | 915 | 915 |
| | $ 12,308 | $ 3,113 | $ 15,421 |

## 13. SEGMENTED INFORMATION: *continued*

Expenditures on property and equipment, intangible assets and depreciation and amortization:

| | 2005 | | 2004 | |
|---|---|---|---|---|
| | **Expenditures on capital assets and other intangibles** | **Depreciation and amortization** | Expenditures on capital assets and other intangibles | Depreciation and amortization |
| Food processing and distribution | **$ 1,735** | **$ 1,580** | $1,698 | $1,612 |
| Real estate and rental properties | **–** | **158** | – | 161 |
| | **$ 1,735** | **$ 1,739** | $1,698 | $1,773 |

Total identifiable assets:

| | 2005 | 2004 |
|---|---|---|
| Food processing and distribution | **$ 22,349** | $23,293 |
| Marketable securities | **27,376** | 10,324 |
| Real estate and rental properties | **2,953** | 3,769 |
| | **$ 52,678** | $37,386 |

## 14. FINANCIAL INSTRUMENTS:

***(a) Fair values:***

As at June 30, 2005 and 2004, the fair values of the Corporation's related party balances were considered undeterminable due to the inability to apply a valuation method or obtain market prices. The fair values of all other monetary assets and liabilities, other than marketable securities (see note 2) approximated their carrying values.

***(b) Credit risk:***

Credit risk arises from the possibility that the entities to which the Corporation provides services may experience difficulty and be unable to fulfill their obligations. The Corporation is exposed to financial risk that arises from the credit quality of the entities to which it provides services.

As at June 30, 2005, five customers accounted for 74%, (2004 – 73%) of consolidated revenues from operations and five customers accounted for 58% (2004 – 56%) of the consolidated accounts receivable. The Corporation believes that there is no unusual exposure associated with the collection of these receivables. The Corporation performs regular credit assessments of its customers and provides allowances for potentially uncollectible accounts receivable.

***(c) Interest rate risk:***

The Corporation is exposed to fluctuations in interest rates with respect to its margin loan, bank loan, long-term debt, and balances due to and from related parties.

***(d) Market risk:***

A substantial portion of the Corporation's income is derived from its marketable securities portfolio and from that of Somerset Properties. The performance of those porfolios and the income derived therefrom is subject to market fluctuations, changes in commodity prices and the performance of the entities whose securities are held. The value of the Corporation's real estate investments are also subject to market fluctuations.

## 15. COMMITMENT:

The Corporation had a royalty agreement with a company of which the chairman of the Corporation is the president but not a shareholder. The royalty agreement extended to June 30, 2004 and resulted in the Corporation having to pay an annual obligation equal to the lesser of:

(i) $360,000; or

(ii) 18% of the gross sales of a wholly-owned subsidiary of the Corporation.

The Corporation fulfilled this commitment as of June 30, 2004, and no payments were made during the year ended June 30, 2005.

Equipment for the Mini Muffin Line has been ordered from Peerless Group. The estimated cost is $300,000 in capital expenditure by October 2005.

Subsequent to year end, the Company entered into a contract to purchase equipment valued at $180,000 USD.

## 16. SUPPLEMENTAL CASH FLOW DISCLOSURE:

***(a) Changes in non-cash working capital:***

| | 2005 | 2004 |
|---|---|---|
| Marketable securities | $ (12,776) | $ (4,646) |
| Accounts receivable | 538 | (558) |
| Inventory | 129 | (682) |
| Prepaid expenses | (136) | 34 |
| Accounts payable, margin loans and other liabilities | 11,702 | 4,221 |
| | $ (543) | $ (1,631) |

***(b) Cash payments:***

The following approximate cash payments were made:

| | 2005 | 2004 |
|---|---|---|
| Interest | $ 1,449 | $ 1,061 |
| Taxes | $ 60 | $ 58 |

## 17. SUBSEQUENT EVENT:

Subsequent to June 30, 2005 the Corporation repurchased 113,000 common shares for cash consideration totaling approximately $111 thousand.

On July 18, 2005, the Corporation extended a loan agreement of $250,000 (note 5b) from a shareholder and former officer of the Corporation for another two years. The principal amount will be due and payable on July 31, 2007, with other terms of the original loan agreement unchanged.

Subsequent to June 30, 2005, a fire at Versa Cold warehouse, an outside storage facility, damaged approximately $275,000 finished goods of a subsidiary. The damage has been reported and is believed by management to be covered by insurance.

# Notes

Notes